By Marcy R. Frost

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Employers often attempt to soften the blow of an employment termination by offering the departing employee a severance package. Unless a union contract, company policy, or individual contract requires a severance payment, such offers by employers are completely voluntary. Except in unusual circumstances, employers should condition any severance package on the signing of a full and effective waiver of any potential claims by the employee. Employers often want to keep the documentation "short and simple," but this article explores some of the nuances of separation agreements that may make a more detailed document more appropriate.

The Older Workers Benefit Protection Act ("OWBPA") amended the Age Discrimination in Employment Act ("ADEA") to address the requirements for an effective waiver of ADEA claims. The ADEA applies to employers with 20 or more employees and protects employees 40 years old or older from discrimination based on age. Pursuant to the OWBPA, an employee whose employment termination is based on individual circumstances must be given 21 days in which to review the agreement before signing it. When the termination is part of an "exit incentive" or "termination program," the 21-day review period is increased to 45 days and the employee must be given age-specific demographics concerning the affected work units. In every situation, the employee must be given seven days after signing the agreement to rescind the waiver of the age discrimination claims. Failure to comply with these and other requirements of the OWBPA can result in a nullification of the employee's waiver of ADEA rights.

The Minnesota Human Rights Act ("MHRA") applies to all Minnesota employers regardless of size. In order to effectively waive a claim for discrimination based on race, color, creed, religion, national origin, sex, marital status, disability, sexual orientation, age, or other protected categories under the MHRA, the employee must be given 15 days after signing the agreement to rescind the waiver of the MHRA claims. Where the ADEA is also applicable, the rescission periods run concurrently. This requirement is unique among state human rights laws. Employers and lawyers from outside Minnesota often overlook the rescission requirement, which makes "borrowing" an agreement from outside Minnesota a dangerous shortcut. The 15-day rescission period also raises issues regarding the timing of severance payments. If payments are going to be made according to a regular payroll schedule, the first payment might be required before the rescission period ends. Payments made prior to a rescission are difficult to recover.

The Equal Employment Opportunity Commission ("EEOC") has challenged many common separation agreement provisions. The EEOC has taken the position that a clause in a separation agreement that prohibits the employee from reapplying for employment with the employer may be a form of retaliation. The EEOC also has declared that language in a separation agreement that purports to waive the right to file a charge with the EEOC, continue the processing of such a charge, or participate in an investigation is unenforceable and itself a violation of the law. Employees, however, can waive their right to pursue damage awards in an EEOC proceeding, and a carefully worded separation agreement can accomplish this. The separation agreement does not need to inform employees of their right to pursue an EEOC claim, but it cannot contain any language that suggests that such a right has been waived. Release, covenant-not-to sue, and non-disparagement provisions should be drafted with this EEOC position in mind.

Section 409A of the Internal Revenue Code and the corresponding Treasury Regulations ("409A") have implications for any form of "deferred compensation," which under some circumstances can include post-termination severance agreements. A provision that allows the employer to accelerate the

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payments would subject the employee to serious tax consequences, even if the acceleration never actually occurs. Unless the agreement provides for all payments to be completed within two and one-half months of the tax year following termination (the next March 15 for most employers), the tax penalties may apply if the termination of employment was voluntary, the amount exceeds a formulaic maximum, the payments extend too far into the future, or continued obligations to the employer are inconsistent with 409A's concept of "separation from service." Although the most serious consequences of 409A fall upon the employee in the form of imputed income, penalties, and interest, employers also face reporting and withholding challenges relating to 409A.

Entire Agreement provisions that are often included in separation agreements as "boilerplate" need to be given careful consideration. Is there an employment agreement or other agreement that requires the employee to keep information confidential or prohibits certain forms of post-employment competition? What about loans or other special agreements with the employee? Sometimes it is to the employer's advantage to state that the separation agreement supersedes any prior agreements, while at other times it is important to make sure that prior agreements are preserved.

Affiliated entities and individuals, such as parent, subsidiary, or sister companies and directors, governors, officers, managers, and co-workers should be included in the release of claims and, if applicable, a non-disparagement clause. Oftentimes agreements include such related entities and individuals within the definition of "Company" or "Employer," but such an expansive definition can lead to problems. An acknowledgment that the employee worked for such a Company or Employer may be interpreted as an admission that the related entities were "joint employers." Also, the inclusion of other entities and individuals as "parties" to the agreement can cause confusion when only the immediate employer is a signatory.

Benefits to the employer other than the release can be obtained, so thought must be given to whether there are other concessions that should be sought. An express agreement to treat business information as confidential often is included where there is sensitive material not covered by any confidentiality agreement. If the severance amount is significant, an employee may be willing to limit post-employment competitive activities. Separation agreements also can include transition or litigation assistance provisions.

Unique circumstances may require special attention in a separation agreement. If the employee is an owner, equity buy-out provisions in a buy-sell agreement may be implicated or a buy-out may be part of the separation package. Employees who serve as officers or directors (or comparable positions in a limited liability company) usually should be required to resign their other positions as part of the severance agreement. Special provisions may need to be included concerning the transition of company vehicles or computers. Certain wage claims cannot be released without public agency participation, so the potential for such claims must be considered. A full analysis of the relationship with the employee is important when structuring a severance package and drafting a separation agreement.

A severance package supported by a well-crafted separation agreement can bring final closure to an employment relationship. A separation agreement that is not tailored to the needs of both the employee and the employer can jeopardize existing rights of the employer or leave the door open for future claims by the employee. If you would like to discuss an appropriate severance offer or need assistance in preparing a separation agreement, contact your attorney at Moss & Barnett.